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COMMENTS ON PROPOSED REGULATIONS REGARDING SPECIAL TREASURY  
OBLIGATIONS OF THE STATE AND LOCAL GOVERNMENT SERIES ("SLGS")  
AFFECTING TAX-EXEMPT BONDS (Docket Number BPD-02-04)

Introductory Background on the Firm

Hawkins Delafield & Wood LLP is a major national bond counsel firm in the tax-exempt bond area, which is headquartered on Wall Street in New York, with offices in Hartford, CT, Los Angeles, CA, Newark, NJ, Sacramento, CA, San Francisco, CA, and Washington, DC. Hawkins has one of the largest and most longstanding national practices in the public finance area, with over 100 lawyers dedicated to public finance and related practices. Since statistics began being compiled in 1980, Hawkins has been bond counsel or underwriters' counsel on more than \$500 billion in aggregate dollar amount of tax-exempt bonds and over 8,000 tax-exempt bond issues. Our clients range from small local school districts to the largest transportation agency in the country and states such as New York and California. We have worked on transactions which range from small plain vanilla general obligation bonds to some of the largest and most complex advance refundings ever undertaken in the municipal market. We and our clients are active users of the SLGS program. We respectfully offer these comments to assist you in preserving and improving the workability and flexibility of the SLGS program.

I. INTRODUCTION TO COMMENTS.

These comments address the Treasury Department's recent Proposed Regulations regarding the special United States Treasury obligations of the State and Local Government Series ("SLGS") which affect tax-exempt bonds. These Proposed Regulations were issued under 31 C.F.R. Part 344, Department of Treasury Circular No. 3-72, 69 Fed. Reg. 58756 (September 30, 2004) (referred to herein as the "Proposed SLGS Regulations" and cited for convenience as "Prop. Reg. §344"). The Proposed SLGS Regulations would amend the existing final Treasury Regulations regarding SLGS under 31 C.F.R. Part 344 (the "Final SLGS Regulations").

## II. EXECUTIVE SUMMARY.

Market reform provisions generally appropriate. In general, we believe that the proposed restrictions on market practices involving uses of the SLGS as cost-free options and the restrictions on the use of the SLGS program in connection with sales or early redemptions of securities to gain yield are appropriate, with one principal caveat noted in the next paragraph. We recommend that the market reform restrictions regarding yield comparability be limited to refunding escrows and that the maturities of the affected securities be taken into account in the consideration of yield comparability.

Recommend preserving ability to receive the benefit of increasing yields during the 60-day period for initial SLGS subscriptions. Specifically, we recommend preservation of the flexibility to cancel and resubscribe for SLGS to receive the benefit of increasing yields during the 60-day period for initial SLGS subscriptions (sometimes referred to as the “float up” option) to further the overriding Federal tax policy of promoting the use of the SLGS program by issuers to the fullest extent possible and reducing the amount of tax-exempt bonds outstanding through the most efficient possible escrows for yield restriction. In this regard, we specifically recommend that this float up option be exercisable on a one-time basis to reduce Treasury’s administrative burdens in this area. We acknowledge the potential need for a fee for this option if Treasury finds it necessary.

Series of Recommendations to Preserve Administrative Flexibility of the SLGS Program. While we recognize the appropriateness of certain proposed market reforms regarding cost-free options and escrow restructurings, we are concerned that, in a number of other respects, the Proposed SLGS Regulations reduce the administrative flexibility of the SLGS program unduly. In this regard, we have a series of modest recommendations to preserve the administrative flexibility of the SLGS program and to try to address the reasons for Treasury’s proposed administrative restrictions in more workable ways to the extent appropriate.

Set forth below are highlights of certain of these administrative recommendations.

- We recommend extending the closing time period for same day pricing of SLGS from 6:00 P.M. Eastern time to 10:00 P.M. Eastern time or preferably Midnight Eastern time in recognition of the decline in trading in the over-the-counter market after 6:00 P.M., the burdens on issuers, bond counsel, and verification agents to finalize verifications, and due recognition of the normal business day on the West Coast and in Alaska and Hawaii.
- We recommend changing the proposed requirement that subscribers certify that issuers have “authorized” the bonds to a requirement that subscribers certify that issuers “intend” to issue bonds (or, alternatively, that issuers “reasonably expect” to issue bonds) in order to accommodate the diverse bond authorization practices of issuers.
- We recommend retaining the flexibility to delay the issue date for SLGS by up to seven days because this flexibility is rarely used and is appropriate.

- We recommend retaining the flexibility to change the size of SLGS by an amount equal to the greater of \$10 million or 10% of the original principal amount because the \$10 million prong of this standard appropriately provides flexibility for smaller issues below \$100 million, which was the stated objective for this rule in the first instance.
- We recommend retaining the flexibility to invest in SLGS from sources of funds which include both gross proceeds of an issue and other amounts which assist an issuer in complying with Federal tax restrictions since there are a number of bona fide circumstances, including a fundamental accounting principle under the Treasury Regulations on the arbitrage restrictions, in which blended investment portfolios including amounts in addition to gross proceeds of tax-exempt bonds properly should be eligible for investment in SLGS.
- We recommend an advance subscription procedure for zero-yielding Time Deposit SLGS for zero SLGS rollovers needed to facilitate Federal tax compliance.
- We believe that the proposed mandatory SLGSafe electronic subscription process for SLGS is constructive and workable.

### III. SPECIFIC COMMENTS AND RECOMMENDATIONS.

#### A. Proposed Restrictions on Certain Market Practices Involving Use of SLGS as Cost-Free Options and Certain Restrictions on SLGS Investments in Connection with Sales or Redemptions of Securities to Gain Yield.

##### 1. Prop. Reg. §§344.2(e)(3) and 344.2(f)(1).

Treasury proposes to restrict certain market practices that Treasury believes may involve inappropriate uses of the SLGS program as “cost-free options” or to derive arbitrage advantages based on relatively infrequent pricing of SLGS. In Prop. Reg. §344.2(f)(1), Treasury proposes generally to prohibit using the SLGS program to create a “cost-free option.” In addition, in Prop. Reg. §344.2(e)(3), Treasury proposes yield certification requirements in connection with the purchase of SLGS with proceeds of the sale or redemption of either open market securities or other SLGS which would require that subscribers must certify that the yield on the SLGS to be purchased does not exceed the yield on such securities to be sold or redeemed. Further, in Prop. Reg. §344.2(f)(1), Treasury proposes to prohibit expressly the purchase of SLGS from amounts derived from the sale or redemption of open market securities if the yield on the SLGS to be purchased exceeds the yield on such securities to be sold or redeemed. Similarly, Treasury proposes to prohibit the purchase of any investments from amounts derived from the sale or redemption of SLGS if the yield on that investment exceeds the yield on the SLGS to be sold or redeemed.

##### 2. Comments.

Subject particularly to our further comments in the next section regarding the recommended preservation of the flexibility to cancel and resubscribe for SLGS to receive the benefit of increasing yields during the 60-day period for initial SLGS subscriptions, we generally believe that the proposed restrictions on market practices involving uses of the SLGS as cost-free options and the restrictions on the use of the SLGS program in connection with sales or early redemptions of securities to gain yield are appropriate. The yield comparability restrictions mainly affect refunding escrow restructurings and seem somewhat inapposite in other circumstances, such as yield-restricted debt service reserve funds. One technical concern about the applicability of the yield comparability provisions is that they appear to lack any consideration of whether the maturities on the affected securities are comparable. For example, if an issuer held a SLGS investment with a five-year maturity in a debt service reserve fund, and such issuer wanted to liquidate that investment in order to invest in a SLGS investment with a ten-year maturity at a higher yield, the mere investment in a longer-term higher-yielding SLGS investment properly ought not trigger the restrictions on yield comparability in connection with sales or early redemptions of securities.

### 3. Recommendations.

We recommend that the yield comparability restrictions under Prop. Reg. §§344.3(e)(3) and 344.3(f)(2) in connection with sales or early redemptions of securities be limited to investments involving restructurings of refunding escrows. We further recommend that the yield comparability restrictions under Prop. Reg. §§344.3(e)(3) and 344.3(f)(2) be amended to include consideration of whether the maturities of the affected securities are comparable so that the yield comparison involves comparable investment scenarios.

#### B. Proposed Elimination of Cost-Free Option to “Float Up” to Receive the Benefit of Increasing Yields During the 60-Day Period for Initial SLGS Subscriptions.

##### 1. Prop. Reg. §§344.2(f)(1)(i); 344.5(c); 344.8(c); and Proposed Deletion of Existing Example under Treas. Reg. §344.2(f)(3)(iv).

As indicated previously, Prop. Reg. §344.2(f)(1)(i) would prohibit the use of the SLGS program to create a “cost-free option.” The present ability to subscribe for SLGS, to cancel those subscriptions freely, and to resubscribe for SLGS at higher yields during the 60-day initial subscription period for SLGS is such a cost-free option. Treasury proposes to delete the existing example under Treas. Reg. §344.2(f)(3)(iv) which permits this free cancellation and resubscription practice. Prop. Reg. §§344.5(c) and 344.8(c) would require that a subscriber for SLGS show that a cancellation is required for reasons other than the use of the SLGS program to create a cost-free option.

##### 2. Comments.

Treasury raised two primary and distinct concerns about the ability of issuers to cancel and then to resubscribe for SLGS to receive the benefit of increasing yields during the 60-day period for initial SLGS subscriptions. First, Treasury raised an administrative concern about its ability to administer large volumes of SLGS cancellations and resubscriptions during periods of

rising interest rates. Anecdotally, a besieged and overloaded facsimile machine at the Treasury's Bureau of Public Debt aptly illustrated this administrative concern. Importantly, Treasury's proposal to make the SLGSafe electronic subscription system mandatory for SLGS subscriptions under Prop. Reg. §344.3 should go a long way towards addressing this administrative concern about processing a large volume of SLGS subscriptions. We believe that the proposal to make the SLGSafe electronic system mandatory for SLGS subscriptions is constructive and workable.

Second, Treasury expressed a concern about the use of the SLGS program to provide a cost-free option and indicated in the preamble to the Proposed SLGS Regulations that it would be impractical to price these options.

We believe that the strong and overriding Federal tax policy to encourage State and local governmental issuers of tax-exempt bonds to use the SLGS program in lieu of open market Treasury securities should outweigh Treasury's concerns about cost-free options during the initial 60-day period for SLGS subscriptions. This strong Federal tax policy should support allowing issuers to "float up" to benefit from increasing interest rates during that time in order to provide the strongest possible incentive for issuers to invest in SLGS. Moreover, particularly given the difficulties in assuring fair market value pricing of open market Treasury securities used in refunding escrows with tax-exempt bonds and the Federal regulatory initiatives in this area, we believe that the stronger Federal policy here should be to maximize use of the SLGS program. The Federal regulatory initiatives involving pricing of open market Treasury securities are exemplified by the 1998 "Global Yield Burning" settlement with the IRS, the SEC, the Justice Department, and 15 major investment banks, which affected over 3,400 tax-exempt bond issues and pricing of associated open market Treasury securities.

### 3. Recommendations.

We recommend that, during the 60-day period for initial SLGS subscriptions, subscribers should be given a *one-time* option to cancel and resubscribe for SLGS at the highest yields in the SLGS rate tables during that 60-day period up until the date of the exercise of that option so as to enable issuers to "float up" to benefit from increasing interest rates. We believe that this proposal would provide significant incentives to maximize use of the SLGS program during periods of rising interest rates. We are concerned that, otherwise, issuers may leave the SLGS program in periods of rising interest rates and invest in open market Treasury securities, which seems to run counter to the overriding Federal tax policy of promoting investments in SLGS instead of open market Treasury securities for yield-restricted tax-exempt bonds. We believe that limiting this float-up option to a one-time option should minimize any remaining administrative concerns with this option. This suggestion recognizes that the proposed mandatory requirement to use the SLGSafe electronic system for SLGS subscriptions largely should ameliorate the administrative issues.

In the preamble to the Proposed SLGS Regulations, Treasury indicated that it had considered allowing use of the SLGS program to provide options if Treasury were compensated appropriately, but that Treasury had determined that it would be impractical to price options at this time. We suggest that if our recommended float up options were limited to one-time options for any particular SLGS subscription, that limitation on the volume of these options should make

it more manageable and practical to price these options. Thus, if Treasury deemed it necessary, Treasury possibly could consider imposing a uniform fee for the use of this one-time option at a prescribed level (e.g., possibly something in the vicinity of .05% to .25% of the principal amount of the issuer's SLGS subscription). This one-time float up option should strike an appropriate balance between providing an incentive to maximize use of the SLGS program and limiting Federal administrative, cost, and planning burdens.

C. Proposed Time Frame for Same Day Pricing of SLGS.

1. Prop. Reg. §344.3(g).

Prop. Reg. §344.3(g) provides that SLGS subscriptions and requests for early redemption must be made between 10:00 A.M. and 6:00 P.M. Eastern time. SLGS rates are those in effect for that day. In the preamble to the Proposed SLGS Regulations, Treasury noted that the 6:00 P.M. closing time generally corresponds to when trading in the over-the-counter market for marketable securities declines in New York.

2. Comments.

In general, the proposal for same day pricing of SLGS subscriptions between 10:00 A.M. and 6:00 P.M. is fairly workable. We have some concern that the 6:00 P.M. closing time may place some administrative burdens and pressures on bond counsel and verification agents with respect to finalizing prices and verifications. This concern is heightened on the West Coast and in Alaska and Hawaii.

3. Recommendations.

We recommend that the closing time for SLGS subscriptions and redemptions be extended to 10:00 P.M. Eastern time or preferably Midnight Eastern time to provide bond counsel and verification agents with sufficient time reasonably to conclude final pricing and verifications for refunding escrows for tax-exempt bonds, with due accommodation of normal business hours on the West Coast and in Alaska and Hawaii. This modest extension of time should present no opportunity for abuse, particularly given that trading in the over-the-counter market for marketable securities declines in New York after 6:00 P.M. Eastern time, as Treasury duly noted in the preamble to the Proposed SLGS Regulations.

D. Proposed Requirement to Certify that an Issuer has Authorized the Issuance of the State or Local Bonds.

1. Prop. Reg. §344.2(e)(2).

Prop. Reg. §344.2(e)(2) would require that, upon starting a SLGS subscription, the subscriber must certify that the issuer has authorized the issuance of the State or local bonds.

2. Comments.

We are concerned that the proposed bond authorization certification requirement may fail to accommodate the widely-varied State and local governmental bond authorization practices among the nearly 50,000 issuers and approximately 15,000 bond issues done annually. This requirement potentially may be inconsistent with some existing State and local governmental bond authorization procedures in which the formal bond authorization is done late in the process after final pricing. We understand that this proposal may represent Treasury's effort to respond to some isolated instances involving SLGS subscriptions without any indication of a real bond issue to be done. We suggest that Treasury address this concern in an alternative manner which may more easily accommodate State and local bond authorization practices.

### 3. Recommendations.

We recommend that the proposed bond authorization certification requirement be modified to require that the subscriber for SLGS certify that the SLGS subscription relates to a State or local bond issue that the issuer *intends* to issue. This certification of intent requirement potentially could draw upon an analogy from a known existing standard involving official intent to issue tax-exempt bonds as a basis for reimbursing prior internal costs under Treas. Reg. §1.150-2. This certification of intent requirement should address fairly Treasury's concern that SLGS only be used for "real" bond issues. At the same time, this certification of intent requirement would provide more flexibility to State and local governments and should accommodate their different bond authorization procedures.

Alternatively, another possible way to modify the proposed bond authorization certification requirement would be to require that the subscriber for SLGS certify that the SLGS subscription relate to a State or local bond issue that the issuer *reasonably expects* to issue. This reasonable expectation requirement also could draw upon an analogy from a known existing standard involving the reasonable expectations test under Treas. Reg. §1.148-1(b) of the Treasury Regulations on the arbitrage investment restrictions.

#### E. Proposed Elimination of Flexibility to Delay Issue Date by Seven Days.

##### 1. Prop. Reg. §344.5(d)(1).

Prop. Reg. §344.5(d)(1) would eliminate the existing rule which permits issuers to change the issue date of SLGS by up to seven days and would prohibit any change in the issue date, absent an express Treasury waiver.

##### 2. Comments.

In general, issuers delay the closing dates of their tax-exempt bond issues only in rare circumstances and only for bona fide reasons. Issuers should have the flexibility and the right to delay the issue dates of SLGS subscriptions by up to seven days. We believe that the existing right to delay the issue date of SLGS by up to seven days has been used infrequently. Moreover, we are concerned that the proposed revocation of the flexibility to extend the issue date of SLGS by seven days may impose a significant burden on issuers who need this flexibility in various circumstances for bona fide reasons having nothing to do with taking advantage of SLGS rates.

Anecdotally, we are concerned that this proposal to prohibit changes in the closing date for SLGS possibly may represent an overreaction by Treasury to a single example of a large transaction in which the closing date was changed.

3. Recommendations.

We recommend that the existing rule which permits issuers to delay the issue date of SLGS by up to seven days be retained because it provides appropriate flexibility, it is used rarely, and it not subject to abuse.

F. Proposed Limitations on Flexibility to Change Size of SLGS Subscriptions.

1. Prop. Reg. §344.5(d)(2).

Prop. Reg. §344.5(d)(2) would reduce the existing flexibility to change the size of SLGS subscriptions. The existing rule permits changes in the size of SLGS subscriptions by an amount equal to the greater of 10% of the original principal amount of the SLGS subscription or \$10 million. Prop. Reg. §344.5(d)(2) would drop the \$10 million prong of the existing rule and thus would limit changes in the size of SLGS subscriptions to no more than 10% of the original aggregate principal amount specified in the SLGS subscription.

2. Comments.

The proposed limitations on flexibility to change the size of SLGS subscriptions would reduce the flexibility presently afforded to issuers with smaller SLGS subscriptions which are less than \$100 million. Here, again, we are concerned that this further proposed restriction on flexibility may have been prompted by very isolated instances of \$10 million changes which Treasury perceived to be inappropriate.

3. Recommendations.

We recommend retaining the existing rule which permits issuers to change the size of SLGS subscriptions by an amount equal to the greater of 10% of the original principal amount of the SLGS subscription or \$10 million because the existing rule provides appropriate flexibility, particularly for smaller issues. We suggest any isolated inappropriate practices involving changes in the size of SLGS might be better addressed under the proposed general anti-abuse rules under Prop. Reg. §344.2(m).

G. Proposed Limitation on Sources of Funds Eligible for SLGS Investments to “Gross Proceeds” of Tax-exempt Bonds Only.

1. Prop. Reg. §344.0(a).

Prop. Reg. §344.0(a) would limit the sources of funds eligible to be used for SLGS investments to amounts that constitute “gross proceeds of an issue.” By contrast, the existing rule provides further flexibility to purchase SLGS investments from sources of funds that either:



(i) constitute gross proceeds of an issue (as defined in Treas. Reg. §1.148-1(b)); or (ii) assist in complying with applicable provisions of the Internal Revenue Code relating to the tax exemption.

## 2. Comments.

We understand that Treasury proposed to limit the sources for SLGS investments to amounts which constitute gross proceeds of an issue because of a concern that the existing rule was ambiguous in permitting SLGS to be purchased from sources which “assist” issuers in complying with the tax-exempt bond rules. We believe that Treasury may not have fully appreciated the administrative flexibility and certainty afforded by the existing rule in many common circumstances facing issuers. Moreover, the need for the existing rule is grounded in part in the technical operation of the Treasury Regulations on the arbitrage restrictions under Section 148 of the Internal Revenue Code. Specifically, the “universal cap” accounting concept under Treas. Reg. §1.148-6(b)(2) basically provides a cap on amounts treated as gross proceeds of an issue based on the outstanding principal amount of the issue. The application of this universal cap concept can have the effect of de-allocating amounts so that they are no longer treated as gross proceeds of issues of tax-exempt bonds and vice-versa. The effects of the universal cap depend on factors which include amortizations of outstanding bonds and fluctuations in valuations of investments. The characterization of funds as gross proceeds under the universal cap may change and such changes in characterization may trigger valuation requirements for purposes of complying with applicable arbitrage investment yield restrictions. Thus, it is important to be able to invest funds associated with tax-exempt bond issues in SLGS to provide greater certainty for compliance with the arbitrage restrictions even if those funds technically may not be gross proceeds at all times as a result of the universal cap.

In addition, many common circumstances exist in which issuers fund refunding escrows, defeasance escrows, or debt service reserve funds from mixed sources of funds. These mixed sources of funds may include proceeds of tax-exempt bond issues, proceeds of taxable bond issues, and other equity funds. In the case of these mixed sources of funding, it may be important to be able to invest all of the sources of funds in SLGS to provide greater certainty to assure compliance with applicable arbitrage restrictions. One classic example here would be debt service reserve funds for pooled clean water revolving fund programs, which typically are funded with both proceeds of tax-exempt bonds and Federal and state grant funds. Arbitrage compliance for these revolving fund programs is very complex and circumstances exist in which it may be easier administratively to invest these funds entirely in SLGS.

Another common kind of circumstance in which it may be helpful administratively to invest funds in addition to gross proceeds of tax-exempt bond issues in SLGS involves taxable bond issues that are part of a series of refundings in which tax-exempt bond issues also comprise some part of the series of refundings. The application of the arbitrage “transferred proceeds” principles under which proceeds of refunded bond issues transfer to and become proceeds of refunding bond issues may make it important to be able to invest in SLGS to assure compliance with arbitrage yield restrictions and to provide greater certainty even when certain amounts technically may be proceeds of taxable issues and thus not gross proceeds. Circumstances involving refundings with taxable bonds may trigger “mark-to-market” requirements for

transferred investments which exposes an issuer to market value fluctuations inherent in open market Treasury securities. This circumstance heightens the need to invest in SLGS with a more certain market value to provide more certainty in Federal tax compliance with applicable arbitrage investment yield restrictions.

In addition, on a related technical point, some ambiguity exists under existing Treasury Regulations regarding when and to what extent proceeds of taxable bonds are treated as gross proceeds of an “issue” for purposes of the tax-exempt bond rules under Treas. Reg. §1.150-1. Specifically, it is unclear technically whether the term “issue” under those regulations includes only tax-exempt bond issues or also taxable issues issued by State and local governments or also taxable issues issued by third parties, such as conduit borrowers or banks, in various circumstances. Thus, for purposes of the SLGS regulations, even the basic rule that amounts must be “gross proceeds of an issue” to be eligible to be invested in SLGS is ambiguous. For this reason, it would facilitate certainty to employ the broader definition of funds eligible for investment in SLGS under the existing rule.

In summary, for the foregoing reasons, the existing flexibility to invest both gross proceeds of tax-exempt bond issues and other funds that may assist an issuer in complying with applicable provisions of the Internal Revenue Code relating to the tax exemption is needed.

### 3. Recommendations.

We recommend retaining the existing rule that provides issuers with the flexibility to purchase SLGS investments from sources of funds that either: (i) constitute gross proceeds of an issue (as defined in Treas. Reg. §1.148-1(b)); or (ii) assist in complying with applicable provisions of the Internal Revenue Code relating to the tax exemption.

Alternatively, if Treasury feels that further specific clarification is needed regarding which sources of funds beyond gross proceeds of tax-exempt bond issues should be eligible for SLGS investments, we recommend permitting the following sources of funds in addition to gross proceeds of tax-exempt bonds to be invested in SLGS: (i) amounts that originally were gross proceeds of tax-exempt bonds, but that are no longer treated as such gross proceeds as a result of the operation of the universal cap on the maximum amount treated as gross proceeds under Treas. Reg. §1.148-6(b)(2); (ii) proceeds of taxable issues and equity funds of issuers or conduit borrowers which are held together with proceeds of one or more tax-exempt bond issues in refunding escrows, defeasance escrows, or parity debt service reserve funds; and (iii) proceeds of a taxable issue which refunds a tax-exempt bond issue or is refunded by a tax-exempt bond issue.

#### H. Recommend Advance Subscription Provision for Zero-Yielding SLGS.

##### 1. Prop. Reg. §344.5(a) and Prop. Reg. §344.10.

Prop. Reg. §344.10 provides in part that the only zero-yielding SLGS available after October 26, 1996 are zero-yielding Time Deposit SLGS that are subject to the general rules for Time Deposit SLGS. Prop. Reg. §344.5(a) provides that subscriptions for Time Deposit SLGS, including zero-yielding Time Deposit SLGS, must be made not earlier than 60 days prior to the

issue date and not later than seven days prior to the issue date (reduced to five days prior to the issue date for SLGS in a principal amount of \$10 million or less).

2. Comments.

In many refunding escrows for tax-exempt bonds, the structure of the investment portfolio requires that amounts derived from maturing securities be reinvested in zero-yielding SLGS at a point in time which is well into the future (e.g., several years) in order to blend down the aggregate yield on the overall investment portfolio to comply with applicable arbitrage investment restrictions. The responsibility to subscribe for these zero-yielding SLGS under the escrow agreement may be placed on bond trustees, refunding escrow trustees, or issuers. In a number of circumstances identified in IRS audits and otherwise, basically “footfaults” have occurred in which the responsible parties have failed inadvertently to make the required reinvestments in zero-yielding SLGS necessary to assure arbitrage yield compliance. We believe that it would be a constructive improvement to the SLGS program to allow issuers to make advance subscriptions for these zero-yielding SLGS.

3. Recommendation.

We recommend that subscribers be permitted to subscribe to zero-yielding SLGS without regard to the general maximum 60-day period in advance of the issue date in which SLGS subscriptions may be made. Alternatively, we recommend that subscribers be permitted to purchase zero-yielding SLGS which by their terms have a “forward” issuance date or effective date. This recommendation would promote Federal tax compliance. In addition, obviously, in light of the zero yields on these SLGS, this recommendation should have no negative economic impact on Treasury.

I. Proposed Mandatory SLGSafe Electronic Subscription Program.

1. Prop. Reg. §344.3.

Prop. Reg. §344.3 provides for a mandatory SLGSafe electronic SLGS subscription process.

2. Comments.

We believe the proposed mandatory SLGSafe electronic subscription program for SLGS should be constructive and workable. We further believe that this mandatory electronic program should go a long way towards addressing many of the administrative concerns that underlie some of the proposed restrictions on the SLGS program.

3. Recommendations.


We recommend that Treasury give all due consideration to the extent to which the mandatory SLGSafe Internet-based electronic program for SLGS subscriptions may ameliorate the need for some of the other proposed restrictions on the flexibility of the SLGS program. As a

general matter, subject only to appropriate security and compliance considerations, we encourage the most “user-friendly” possible access to SLGSafe. We particularly want to underscore our previous point that this administrative streamlining ought to enable Treasury to minimize administrative burdens, particularly with facsimile transmissions and monitoring of SLGS subscriptions, and thereby to accommodate our recommended provision which would allow issuers to “float up” to receive the benefit of increasing interest rates during the 60-day period for initial SLGS subscriptions. We stress that our float up option recommendation would maximize participation by issuers in the SLGS program during periods of rising interest rates to the fullest extent possible in furtherance of the overriding Federal tax policy for the SLGS program.

IV. Conclusion.

We appreciate the opportunity to comment on the Proposed SLGS Regulations. Please feel free to contact the undersigned tax partner, John J. Cross III, regarding any questions about these comments. Mr. Cross’s phone number is (202) 682-1487 and his electronic address is [jcross@hawkins.com](mailto:jcross@hawkins.com). In addition, please feel free to call any of the other tax partners at the firm regarding these comments.

HAWKINS DELAFIELD & WOOD LLP

By:   
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